

**DEPARTMENT OF STATE REVENUE
REVENUE RULING # ST 97-01**

August 11, 1997

NOTICE: Under IC 422-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

- I. Sales and Use Tax -- Taxation of prescription drug samples
- II. Sales and Use Tax -- Taxation of promotional materials

STATEMENT OF FACTS

Corporation A is a manufacturer of prescription and nonprescription drugs. As part of its business Corporation A distributes samples of its prescription drugs ("drug samples") to doctors, hospitals and other health care providers around the country, which, in turn, distribute these drug samples free of charge to their patients. Like all of its prescription drugs, Corporation A's drug samples are manufactured in conformity with strict federal laws, regulations and guidelines, including requirements on how they are to be packaged, labeled and distributed.

Drug samples generally consist of the pharmaceuticals, packaging materials and product literature. The tangible personal property that is incorporated into these samples may be purchased by Corporation A from in-state or out-of-state vendors. The drug samples that Corporation A distributes may be produced and/or handled by Corporation A in one of three different ways:

- (1) Corporation A will purchase bulk products (raw materials) from suppliers, which Corporation A will then manufacture or process and package into finished samples. The manufacturing, processing and/or packaging may take place in Indiana and/or elsewhere.
- (2) Corporation A will purchase bulk pharmaceutical products (i.e., pulvules, tablets, ointments, etc.), which Corporation A will then package into finished samples in Indiana and/or elsewhere. For example, Corporation A may purchase bulk finished product from its foreign affiliate and then perform further processing by packaging it into sample form at an Indiana plant.
- (3) Corporation A will purchase finished, packaged samples ready for distribution.

All of Corporation A's drug samples--regardless of whether they fall into the first, second or third scenario described above--are eventually delivered to and stored in one of Corporation A's Indiana warehouses. There, pursuant to shipping orders, Corporation A warehouse personnel withdraw the drug samples from storage, opening the cartons in which the samples are stored and removing the correct quantity of drug samples, if necessary, and then package, label and ship the samples. Samples may be shipped by Corporation A from Indiana to Corporation A employees for distribution to health care providers or others; or samples may be shipped directly from Indiana to health care providers and others.

Therefore, tangible personal property incorporated into or constituting Corporation A's drug samples may be:

- (1) manufactured or processed (including packaged) in Indiana, and/or
- (2) stored in Indiana

at some time prior to its ultimate distribution by Corporation A as a drug sample.

DISCUSSION -- ISSUE I

The question posed in this issue is whether the tangible personal property that is incorporated into or constitutes prescription drug samples is subject to Indiana sales/use tax. The taxpayer has presented three different methods used to distribute drug samples. In the first method, Corporation A purchases bulk products (raw materials) from suppliers, which are then manufactured into finished samples. In the second method Corporation A purchases bulk pharmaceutical products (pulvules, tablets, ointments, etc.) which are then packaged into finished samples. In these two methods, Corporation A is entitled to the manufacturing exemption found at IC 6-2.5-5-6. Thus, the tangible personal property that is manufactured, processed and/or packaged into finished prescription drug samples is exempt from Indiana sales/use tax. IC 6-2.5-3-4 provides that if a person issues an exemption certificate for the acquisition of tangible personal property and subsequently uses, stores, or consumes that property for a nonexempt purpose, then the person shall pay the use tax. IC 6-2.5-3-2 provides that use tax is due only on tangible personal property stored, used, or consumed in Indiana.

RULING

The Department rules that Corporation A is entitled to an exemption from Indiana sales/use tax on the tangible personal property that is incorporated or processed into or constitutes prescription drug samples, including packaging, that are ultimately distributed or shipped by Corporation A to health care providers or others outside of

Indiana. Corporation A is subject to Indiana use tax on the purchase or the storage, use and consumption of prescription drug samples and the materials incorporated therein (including without limitation, the raw materials, finished legend drug samples, and packaging) that are ultimately distributed or shipped by Corporation A to health care providers or others in Indiana.

ISSUE II

Corporation A purchases from in state and out of state vendors finished, packaged drug samples ready for distribution, promotional materials and literature, such as pens, mugs, notepads, reprints of articles on its products, and other promotional materials, for distribution to health care providers. All of these finished, packaged drug samples, promotional materials and literature acquired from vendors registered to collect and remit Indiana sales/use tax were purchased pursuant to a direct *pay* permit. All of these promotional materials and literature are delivered to Corporation A at its Indiana warehouse, where they are stored. Corporation A's field representatives from around the country regularly submit orders for promotional materials and literature for their use in calling on health care providers and others. Pursuant to these orders, Corporation A's Indiana warehouse personnel open the cartons in which the promotional materials are received by Corporation A, remove the correct quantity of requested promotional items, and then pack, label and ship those items to Corporation A's field representative. Corporation A's field representative uses those items in calling on health care professionals and others around the country. Corporation A's counsel apparently argues that its promotional materials should be excepted from use tax under the definition of "storage" as discussed by the Indiana Tax Court in *Miles, Inc.*. The court concluded in that case that the activities of storing, incidental handling, and transporting the property cannot be taxed as "uses". The Tax Court in *Miles* did not define "use"; however, the Tax Court in *U.S. Air, Inc v. Indiana Department of State Revenue*, 623 N.E.2d 466 (1993) held that the storage exception limits and qualifies the meaning of "use". The Court concluded that limiting the "storage" exception to property previously identified for shipment out of Indiana is too narrow. The Tax Court did not establish what amount of activity constitutes "use".

In view of the fact that the Tax Court has included the wording "incidental handling" within the "storage" exception, the Department concludes that the activities of unpacking, sorting, repackaging, labeling the package and transporting the product out of state are "incidental" activities in connection with the "storage" exception. The Taxpayer is cautioned, however, that any "use" beyond unpacking, sorting, repackaging, labeling the package and transportation out of state will not be exempt under the "storage" exception.

RULING

The Department rules that Corporation A has no Indiana sales or use tax liability with respect to the purchase or the storage of ready to distribute drug samples, promotional literature, pens, mugs, notepads, reprints of articles on its products, that are ultimately distributed or shipped to health care providers or others outside of Indiana, provided the ready to distribute drug samples, promotional literature and promotional materials are only received, stored, unpacked, sorted, repackaged, the package labeled and the items transported to locations out of state. The Department need not address the application of IC 6-2.5-3-2(d) at this time.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situation may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in a statute, a regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.